

# Contents

|   |           |
|---|-----------|
| <i>List of Tables</i>                                   | ix        |
| <i>List of Figures</i>                                  | xi        |
| <i>Preface</i>  | xii       |
| <i>List of Abbreviations</i>                            | xv        |
| <i>Acknowledgements</i>                                 | xvii      |
| <b>1 The Old and the New Political Economy</b>          | <b>1</b>  |
| From the old to the new political economy               | 2         |
| Institutions and organizations                          | 8         |
| Different types of state                                | 12        |
| Different types of markets                              | 16        |
| Interactions between state, organizations and markets   | 22        |
| <b>2 Theories of Market and Government Failures</b>     | <b>24</b> |
| Market failures   | 25        |
| Government failures                                     | 28        |
| Parallels between market and government failures        | 37        |
| The relevance of theories to East Asia                  | 38        |
| Conclusion  | 43        |
| <b>3 Financial Crises: Cases of Market Failure</b>      | <b>45</b> |
| Financial globalization                                 | 47        |
| Financial liberalization policies                       | 48        |
| Financial crises in industrial and developing countries | 50        |
| Why failures in financial markets?                      | 57        |
| Lessons from financial crises                           | 63        |
| <b>4 The Asian Financial Crisis</b>                     |           |
| <i>A. S. Bhalla and D. M. Nachane</i>                   | <b>65</b> |
| Key features of the crisis                              | 66        |
| Theoretical explanations                                | 73        |
| Diagnosis of the crisis                                 | 76        |

|  |            |
|--|------------|
| Role of the IMF in the crisis  | 78         |
| The impact of the crisis   | 82         |
| Conclusion   | 90         |
| <b>5 The Impact of the Asian Crisis on China and India</b>                       |            |
| <i>A. S. Bhalla and D. M. Nachane</i>  | <b>92</b>  |
| Vulnerability indicators   | 94         |
| Trade impact   | 105        |
| Impact on capital inflows  | 110        |
| Impact of domestic policies  | 117        |
| Impact on the future of reforms  | 117        |
| Need for financial reforms   | 121        |
| Conclusion   | 125        |
| <b>6. State Enterprises in China and India:<br/>A Case of Government Failure</b> | <b>127</b> |
| The soft-budget constraint   | 127        |
| Excess labour or overstaffing  | 130        |
| State enterprises in China and India   | 132        |
| The soft-budget constraint in Chinese<br>state-owned enterprises (SOEs)          | 137        |
| The soft-budget constraint in Indian public-sector<br>enterprises (PSEs)         | 151        |
| Conclusion   | 161        |
| <b>7 Conclusion: Implementation Failures</b>                                     | <b>162</b> |
| Strategy/policy design   | 166        |
| Other implementation problems  | 169        |
| Conclusion   | 174        |
| <i>Notes</i>   | 175        |
| <i>Bibliography</i>  | 182        |
| <i>Author and Name Index</i>   | 214        |
| <i>Subject Index</i>   | 217        |

# 1

## The Old and the New Political Economy

In the 1950s and 1960s it was rare to find any mention of government failures or of national or global governance. Economic policies and government intervention were justified to overcome market failures or imperfections. In the world of today, the opposite view prevails: that is, almost all economic ills are ascribed to government failures and faulty macroeconomic and sectoral policies. A shift towards a market system involves competition and incentives which are seen as driving forces towards efficiency in resource allocation and use, as well as accelerated economic growth.

This chapter examines the pros and cons of the old and the new political economy of development and its relevance to public policy in developing countries. It discusses different forms of the state and its agents, namely, government and bureaucracy. Parallel to this analysis, one needs a corresponding analysis of different types of markets. We argue that markets left to themselves cannot contribute to growth and equity. Government interventions are essential to overcome market failures and to 'guide' markets towards broader development goals. As we shall discuss in Chapter 7, failures occur not only under non-market systems but also under market systems; most failures under the old and the new political economy frameworks can be attributed to poor design and/or implementation of public policies and programmes as well as private strategies of firms and corporations. It is, therefore, unfair to attribute the blame entirely to governments and public agencies.

Much of the literature uses the terms 'state' and 'government' interchangeably although the two are distinct. In fact, the concept of the 'state' is much broader and also more complex and problematic (see Evans *et al.*, 1985). The state refers to 'a set of institutions that possess the means of legitimate coercion, exercised over a defined territory and

its population, referred to as society. The state monopolizes rule making...through the medium of an organized government' (World Bank, 1997c, p. 20). Lal and Myint (1996, p. 305) note two opposite views of the state: *the civil association* view which defines the state as custodian of laws which facilitate 'individuals to pursue their own ends' and the *enterprise* view which sees it as a 'manager of an enterprise seeking to use the law for its own substantive purposes...'. Our concern in this book is somewhat narrowly focused on the agents of the state – political leaders, government and bureaucracy – rather than the state itself.

## FROM THE OLD TO THE NEW POLITICAL ECONOMY

Under the old political economy framework the role of the state in promoting social welfare was clearly recognized; so were such factors as historical tradition, social structures and institutions, in the shaping of economic policies and their implementation. As Meier (1993) notes, under the old political economy (OPE) framework, which was in vogue in the first few decades after the Second World War, the state and government bureaucracy were benevolent institutions working for the public good. Their role was to overcome market failures which explained poor development performance. The state was traditionally associated with a *rational* entity working for the maximization of social welfare.

The protagonists of the new political economy view of development (NPE) start with the premise that government failures are the villains of the piece and that free functioning of markets and competition are preconditions for the success of economic policy. The NPE paradigm postulates that the state has extended its role and influence far beyond what the norms of efficiency and rational resource allocation would dictate. The rent-seeking behaviour of politicians and bureaucrats is believed to have led to an overextension of the state with a consequent waste of resources, economic inefficiency and corruption.

In the NPE framework, most production of goods and services is left to markets in which producers offer their wares and consumers exercise their preferences and make choices. Economic reform measures adopted by many developing countries in the past several years are designed to diminish and redefine the role of the state by promoting privatization and enhancing the role of the markets in the allocation of resources. There is a growing trend towards market liberalization within the framework of stabilization and structural adjustment policies in developing countries and in the economies in transition in Central and Eastern

Europe. Markets and competition are looked upon as an effective framework for organizing the production and distribution of goods and services although their economic and social costs are increasingly debated. Nevertheless, in situations where subsistence production is significant, markets alone will be even more inadequate (Bhalla and Reddy, 1994; Stiglitz, 1997a). This has not been recognized perhaps partly because of the sudden collapse of the communist regimes, which was taken as a vindication of the superiority of market forces.

In the countries of the erstwhile Soviet bloc, the OPE view has been equated with a state apparatus and bureaucracy responsible for government policy interventions and their implementation. In the early 1990s the people of the former Soviet Union and Central and Eastern Europe rejected this state apparatus and bureaucracy as an effective instrument of choice of goods and services. The fall of communism has led to renewed attacks on government control and ownership of resources. Under communism the state apparatus in these economies extended far and wide. The government and state bureaucracy is known to have failed to work for the public interest and social welfare. State control over production did not result in the production of goods and services of sufficient quantity and quality to satisfy consumer requirements. In the name of social welfare the state bureaucracy often assumed inordinate powers leading to corruption and malpractices.

There is a tremendous mismatch in the production of goods and services between the choices made by the state bureaucracy and the preferences of the consumers. There is a growing feeling that whenever the bureaucracy makes these choices for consumers, it makes the wrong choices because unlike the market, a bureaucracy tends to be cut off from the valuable information and feedback that consumers provide on their preferences for goods and services. (However, this judgement is not peculiar to the communist environment; even in the capitalist environment, many bureaucratic choices can turn out to be disaster (see Chapter 2).

### **Features of the New Political Economy**

The NPE has been defined as a 'neoclassical economic theory of politics' analogous to 'neoclassical economic analysis' (see Meier, 1991, p. 5). It argues in favour of a minimalist state on the grounds of directly unproductive activities of the state and rent-seeking behaviour of public agents and bureaucrats (Bhagwati, 1982; Buchanan *et al.*, 1980; Findlay, 1991; Krueger, 1974; Srinivasan, 1985). Unproductive but profit-seeking activities include rent-seeking but also much more; for example, all

price distortions, tax and tariff evasion, smuggling, bribery, corruption, black markets, and so on (Bhagwati, 1982; Krueger, 1974). While Krueger was interested mainly in rent-seeking activities through trade restrictions, Bhagwati broadened the analysis to include all sorts of economic activities in which rent-seeking resulted from government restrictions which enable bureaucrats, industrialists and private individuals to generate private income (rent) from such controls.

Rent-seeking associated with government intervention is distinct from any rents captured by individual economic agents in pursuit of profit-making (monopoly rents, for example). The state-induced rents are *artificial* in the sense that resources spent in generating and capturing them are a social loss since no resource creation (only reallocation) is involved (Chang, 1994a, pp. 27–31).

The NPE paradigm attributes failures to implement public policy to rent-seeking because governments are assumed to act on behalf of particular interest groups rather than the public welfare. They deliberately introduce public interventions to maximize economic gains for these groups and ensure their distribution as well as power among them.<sup>1</sup>

Rent-seeking will influence administrative behaviour of implementors negatively because it leads a civil servant to rank accountability very low on his/her personal agenda. Moreover, it is reported that countries which receive the major share of their revenues through rents, realized through the export of commodities such as oil or other valuable minerals, are facing the same problem of lax attitudes towards state funds.

Rent-seeking by government influences the administrative costs of enforcement of policies. Krueger (1993) notes that such rent-seeking creates a deadweight cost. But there can also be positive and growth-inducing aspects of rent-seeking behaviour of governments. The South-east and East Asian experiences show that rent-seeking can be devoted by governments to growth and public welfare. The governments created rents to increase investment to fuel growth rather than to benefit a few private and vested interests. Chang (1994a) argues that in late-industrializing countries market mechanism alone could not provide adequate rents. Decline in barriers to trade and big reductions in transport costs, *inter alia*, prevented such rents. The nature of new industries, the high investment costs and the risk involved necessitated government intervention to create rents for early entrants.

Rent-seeking behaviour is not peculiar to governments and the political process; it is equally common in the private sector. Private organizations may deliberately make distorting decisions in order to seek rents and limit competition from outsiders (Boycko *et al.*, 1996;

Edlin and Stiglitz, 1995; Stiglitz, 1997a). Streeten (1993) gives the example of private allocation of contracts to sub-contractors leading to rents in the same way as import quotas. When barriers to entry are high, private-sector firms become monopolistic and charge prices higher than what the production costs would dictate. Thus, to use Adam Smith's phrase, this reflects 'the businessman's conspiracy against the public'. In such situations, government intervention through anti-monopoly legislation may actually reduce unproductive activity and raise output through greater competition. The relevant question is whether governments or markets lead to greater net negative result, when rent-seeking is common to both market and government failures.

Toye (1991a, p. 321) notes two major features of the NPE: (a) 'an unrelievedly cynical view of the state and a sharp disjunction between that view and the political requirements for the adoption of liberalization policies in the economic sphere', and (b) 'the exclusion of *international* economic and political factors from the frame of analysis'. In an interdependent globalizing world of today it is unrealistic to ignore influences of such international bodies as multinational corporations, international banks and development institutions on changes in policy in developing countries. Toye also questions the generally held view that the rent-seeking literature provides the foundation for NPE. The pressures of interest groups in the political process need not always be negative. These groups have been interpreted as equivalent to competitive process in the political field, which ensures consensus and compromise in coalition building. Under the NPE, however, interest groups and competition among them are seen as negative agents which destroy public interest and lead to political fragmentation.

The relevance of the NPE (developed initially in the context of advanced market economies) to developing countries is a matter of some controversy. While Findlay (1991) asserts its universal application, Grindle (1991) argues that its application to public policy making in developing countries is of a rather limited value. She draws a distinction between the 'state-centred' and 'society-centred' view of public policy making. Society-centred political economy models depict competition of interest groups as a threat to government to respond through rational economic policies. On the other hand, the 'state-centred' view poses no such threat since politicians or the political elite are assumed to be as rational as the voters. It is only the state-centred view that is relevant to developing country situations. The 'society-centred' view has limited validity in developing countries because public policy making is generally much less transparent and more closed than in developed countries

Table 1.1 Characteristics of the old versus the new political economy

| <i>Old Political Economy (OPE)</i>  | <i>New Political Economy (NPE)</i>   |
|---|--|
| Market failures are responsible for poor outcome of economic policy                 | Government failures are responsible for poor outcome of economic policy.   |
| Government is a benevolent institution working for the public good                  | Market, deregulation and prices will lead to efficiency and maximum economic/social good.                                    |
| Government intervention is efficient  | Government intervention is inefficient   |
| Interest groups are beneficial and can help promote political consensus             | Interest groups are harmful as they promote rent-seeking   |
| State ownership and control of private enterprise is necessary for equitable growth | State ownership (especially in industries where private enterprises can do better) distorts markets and causes inefficiency. |

(Grindle and Thomas, 1989). The above argument is based on the assumption that interest groups in developing countries are weak and have limited access to the state. As a result, public policy making is centred in the high echelons of government.

This view contrasts Bardhan's (1984) which explains rent-seeking in India through vested group interests.

A contrast between the OPE and the NPE is summarized in Table 1.1 which depicts the characteristics of each.

## A critique

The black and white view of state versus markets is clearly exaggerated. The recent development debate seems to have over-romanticized the successful role of the private sector in promoting growth and reducing inefficiency. As noted above, the fall of socialist governments in the former Soviet bloc has encouraged some to believe that history has given a clear verdict in favour of capitalism and free enterprise. If state and bureaucracy have failed, does it follow that the instrument of markets and *laissez-faire* is necessarily superior? We argue that it does not for the following reasons.

Firstly, in the so-called market economies, limitations of the market have become clear. Stiglitz (1997a) distinguishes between 'traditional'

market failures (for example, externalities and public goods) and the 'recent' analysis of market failures (concentrating on innovation and technology development, information imperfections, absence of markets, and their imperfections when they exist, as is reflected in unemployment, monopolistic situations, and so on) (see Chapter 2). The market for the development of technology may fail, thus calling for government intervention. There may be other market limitations – equity, environment and similar other long-term considerations do not enter the balance sheet. These limitations have led to serious consequences in terms of the pitiable conditions of the poor, homeless and minorities, local and global environmental degradation and the neglect of human resources development.

Secondly, government intervention may be essential to make markets function more effectively. In developing countries, markets function poorly for lack of institutions, social norms and human behaviour (Basu, 1986, 1992). Government has a role to play in introducing appropriate property rights and legal norms. (Social norms and human behaviour at any given point of time would be the result of historical and cultural heritage.) The role of the government may also remain important for the alleviation of poverty and ensuring equity through income transfers or redistribution of incomes. The government role cannot be replaced easily in the provision of public goods and services such as health and education, the maintenance of law and order, building and maintaining infrastructure and environmental protection. It should also be noted that in many developing countries a large proportion of the population is engaged in subsistence production outside the market. In this case the state and social organizations will need to be relied upon to channel goods and services to these people. Even where markets exist, a regulatory framework and legal norms need to be provided by the government for their efficient functioning. The extent to which the outcomes of public policy will actually contribute to these objectives will largely depend on the nature and type of the state (see below). Furthermore, the increasing transitional costs of globalization and economic interdependence between economies can enhance, not diminish, government's role (see Rodrik, 1996a, 1997).

Finally, privatization, which is defended by the protagonists of markets, may be as distorting as a government monopoly. It may not necessarily offer lower prices to consumers. Stiglitz (1997a, p. 85) notes: 'There is some evidence that, insulated from competition, private monopolies may suffer from several forms of inefficiency and may not be highly innovative.'

## INSTITUTIONS AND ORGANIZATIONS

A distinction between 'institutions' and 'organizations' is considered crucial in a study of transaction costs (North, 1990). While institutions provide a framework and rules of the game, organizations refer to groups of individuals guided by common purpose and objectives. The latter are agents of institutional change. The new institutional economics (NIE) provides a framework to explain the role of institutions and norms in reducing information and transaction costs to improve economic performance. North (1990) notes their role in reducing uncertainty and providing stable though not necessarily efficient social structures. It is the economic and social institutions rather than markets or governments whose imperfect operation constrains growth in productivity and efficiency (Harriss *et al.*, 1995).

The role of institutions and organizations as well as their interrelationships are important especially in developing countries because they reduce transaction costs, provide incentives which can enhance efficiency, and avoid or resolve conflict (Stern and Stiglitz, 1997). However, conflicts can be resolved only through partnerships and incentives for cooperative (rather than conflictual) behaviour (for example, partnership or relations between workers, management and government). There is a possibility, however, that while institutions lower transaction costs, the design and establishment of new institutions may incur high transaction costs since it involves risk and uncertainty. Furthermore, institutional rigidities exist; generally institutions take long to adapt to changing economic circumstances. Stern and Stiglitz (1997) note that all institutions may not meet the current needs of the economy, and can in fact, hinder change. But generally, even when legal structures and institutions are weak, social sanctions can help strengthen their enforcement (as for example, in East Asia).

North (1990, p. 27) notes that 'costliness of economic exchange distinguishes the transaction costs approach from the traditional theory'. Transaction costs have also been seen simply 'as a way of describing the causes of market failure' (Khan, 1995, p. 74). Since transaction costs occur under both public and private institutions, alternative institutions need to be identified to lower these costs in order to improve net social benefits. The relevant issue then is transaction cost difference between state (government) intervention and non-intervention. It is possible that 'intervention with rent-seeking may have lower overall transaction costs than *laissez-faire* with lower rent-seeking' (Khan, 1995, p. 75).

While there is continued debate on the precise nature of the state role and government intervention, nobody will deny the need to re-define this role in the light of new development paradigm and national and global governance. While in the old political economy framework the state was justified as a custodian of social justice, under the new framework it can be defended to correct market failures. Thus public policy decision-making and implementation may be intended to promote efficiency by eliminating price distortions, promoting competition by breaking down monopolies, and developing and fostering institutions which strengthen the functioning of factor and product markets.

In writing on the role of investment and profits on East Asian industrialization, Akyüz and Gore (1994) note quite rightly that the 'attempt to isolate economic effects which can be attributed to government, as against the market, is misguided'. Datta-Chaudhuri (1990, p. 38) notes that the dichotomy is 'fake' because 'in a changing world the required institutional changes in markets do not always take place automatically'. The state can promote 'the right kind of market institutions' and 'where market signals alone are not effective guides to desirable action, appropriate nonmarket institutions are required to be created'. In reality, development cannot be achieved either by the private sector alone, or by the state sector alone. There is a role for both. An early World Bank Report (1991, p. 1) states:

markets cannot operate in a vacuum. They require a legal and regulatory framework that only governments can provide. And at many other tasks, markets sometime prove inadequate or fail altogether. This is why governments must, for example, invest in infrastructure and provide essential services to the poor. It is not a question of state or market: each has a large and irreplaceable role

There is no agreement yet on the *precise* assignment of roles and allocation of responsibilities between the state and the market. As Krueger (1990, p. 17) has noted, 'an economically efficient division of economic activity between public and private sector will be based in part on the administrative and organisational requirements of the two alternatives'. Fishlow (1994, p. 1830) states: 'what we lack are a full set of rules for determining the appropriate form and changing role of governmental policy'.

In the final analysis, the *quality* of government (as distinct from its *extent*) and responsibilities will determine its positive or negative role, which can be judged in terms of the quality of policy design and success in the implementation of policies and programmes (see Chapter 7). This can be illustrated by the experience of policy formulation in post-war Japan (1953–1973). Gore (1994) notes how government policy in Japan was formulated taking due account of the views of the business community, the main engine of economic activity. Cooperation between business and government facilitated implementation of policies. Government policy was characterized by both realism and flexibility. For example, although a competitive policy was encouraged, the government tempered competition in the case of small businesses which were exempted from anti-monopoly laws.

### **Role of social organizations**

Social organizations (non-political and non-governmental institutions – so-called civil society) can help overcome market inefficiencies besides providing checks and balances on the state. Some *laissez-faire* economists (for example, Coase (1960) argue that market inefficiencies can be resolved through collective action of individuals in the form of a social organization rather than through government intervention. This argument has been questioned by Dutt *et al.* (1994, p. 5) on the grounds that large transaction costs, free-rider problems and revealed preferences of individuals will make it difficult to achieve private optimal solution. Social organizations, like government entities, may also suffer from narrow self-seeking interests which would lead to irrational economic outcomes.

Some of the social organizations may be state-induced; they are promoted to take over some functions hitherto carried out by the government. This is the case of many recent associations in China. In post-Mao China, the Chinese Government encouraged the creation of semi-official and popular social organizations like the Self-Employed Workers' Associations and Private Entrepreneurs' Associations for fulfilling different objectives, namely, regulating the market, social welfare and consultation in policy making (Howell, 1994). It has been noted that in Xiaoshan (China), the local government and the Association of Science and Technology jointly tackled the problem of land reclamation. The emergence of these associations is expected to achieve simultaneously the objectives of improved state performance, greater equity through provision of social welfare and greater popular participation in decision-making which in turn, is expected to improve the performance

of the Chinese State. In Indonesia and Malaysia the existence of *kelompok* (or small cooperatives) is noted to promote collective action (Barlow, 1999).

Some non-political organizations (for example, farmers' movements in India) may also emerge more spontaneously as a response to economic and political circumstances. In India the new farmers' movements represent social groups created to fight for their economic and social rights and benefits. As distinct from the old peasant movements in India, the focus of new farmers' movements is not land but agricultural prices (Byres, 1994a). Their main objective is to obtain more remunerative input and output prices, particularly the procurement prices, for farmers. To press their case *vis-à-vis* the government, the movements in different states in India have agitated by blocking the food transportation (both rail and road) system, blocking access to politicians in villages, and withholding crops from markets in order to raise prices (Brass, 1994).

Of course, motivations of farmers' movements varies from state to state in India. In the Punjab, it is noted to be a reaction to a gradual erosion of prosperity brought about by the Green Revolution. Commercialization of agriculture leads to market integration of surplus-producing medium and small farmers. They are increasingly vulnerable to input and output price fluctuations. As a result, the Punjab farmers' demands include lower input prices, higher procurement prices, and crop insurance schemes. The farmers' movement in Gujarat on the other hand, seems to be linked to an integration of rural and urban commercial interests.<sup>2</sup>

In both industrial and developing countries traditional forms of civil society (labour unions, chambers of commerce, industry associations) and new forms of community organizations (for example, micro credit associations and other local community organizations) are engaged in the tasks of mitigating the economic and social hardships and 'new' poverty resulting from social exclusion and economic globalization (see Bhalla and Lapeyre, 1999).

Below we shall discuss different forms of the state, markets and non-governmental social organizations to show that a dichotomy between the state and market is misplaced. There is a place for all these three institutions. We argue that a *synthesis* is required between the above three institutions. In this synthesis, advantages of the market need to be harnessed fully. But society must find a way to overcome the limitations of the market by correcting its equity-blindness, its indifference to environmental 'externalities' and its preoccupation with the short term (see Chapter 2).

## DIFFERENT TYPES OF STATE

In the economic literature the state has been defined and characterized differently depending on the positive or negative view of it, its goals in terms of public (or national) interest versus that of interest groups, its autonomy from interactions with society, and so on. The *degree* and *quality* of state intervention in economic activity is another criterion for judging its nature. Bardhan (1991b, pp. 109–10) notes that in the bulk of the neoclassical literature the emphasis is on the extent of state intervention, particularly its harmful effects rather than its quality. He goes on to state that ‘almost all states in developing countries, successful or otherwise, are interventionist, and the important issue is not really the extent but the quality of that intervention’. The nature and quality of such intervention will vary between states. Generally the quality of state intervention is likely to be higher in states that pursue the collective good of citizens than in others which are self-serving. Having mentioned some criteria governing state quality, we now briefly discuss the different types of state discussed in the development literature.

### ‘Soft’ v. ‘hard’ state

Ever since Myrdal's *Asian Drama* (1968) typologies of different types of the state have been presented. Myrdal referred to the ‘soft’ and ‘hard’ states. The ‘soft’ states are those ‘where national governments require extraordinarily little of their citizens. There are few obligations either to do things in the interest of the community or to avoid actions opposed to that interest’ (p. 896). These ‘soft’ states are further characterized by ‘low level of social discipline’ and high level of corruption, tax evasion and black marketeering (p. 894). In contrast, the ‘hard’ states are those in which corruption and tax evasion are less marked. These states may be dictatorial or democratic, but they are characterized mainly by the greater ability to implement economic policies to promote rapid economic growth and social welfare.

States can become strong or hard through a high level of ‘social control’ which makes possible surplus accumulation. Three preconditions of a hard state are: *compliance* (of the population to state's demands), *participation* (in state-run institutions), and *legitimation* (acceptance by the citizens of the state's authority and their approval of state goals) (see Migdal, 1988). The differences in the states' capabilities over time and space can be explained in terms of the degree to which these preconditions are met. Poor enforcement of a state's rules

and laws and failures in implementation of its policies and programmes may be seen as its weakness caused by the lack of fulfilment of one or more of the above preconditions.

The strength of the state is also determined by the nature and types of social structures under which the state operates. A hard state suggests a harmonious social structures whereas a weak state is indicative of social conflicts among various interest groups. Furthermore, centralization of power can be an important ingredient for the making of a hard or strong state. According to Migdal (1988, p. 34), 'the highly centralized and the more diffused can be considered "strong" because the overall level of social control is high'. Migdal concludes with what he calls 'sufficient conditions for creating strong states', namely, social dislocations leading to weakening of existing patterns of social control, existence of a serious external military threat which changes the risk calculus of state leaders, the basis for an independent bureaucracy, that is, 'the existence of a social grouping with people sufficiently independent of existing bases of social control and skillful enough to execute the grand designs of state leaders' (p. 274), and skillful leaders favouring strong state control.

#### **Autonomous vs. factional state**

Lal and Myint (1996) have developed alternative models of the state, classifying it into two broad groups, (a) autonomous and (b) factional. The autonomous state follows its own objectives whereas a factional state represents some sort of collective decision-making. The autonomous state is further divided into the 'predatory' (absolutist or 'bureaucratic authoritarian') and 'guardian' state. The autonomous state may be based on a one-party system which enables it to ignore interests other than its own. The 'absolutist' or 'predatory' state is not confined only to the erstwhile communist countries. It also depicts the situation in many developing countries where the state indulged in rent-seeking and exploitation of its citizens. To quote Meier (1993, p. 383):

'an underdeveloped economy has given rise to an overextended state and to a negative or exploitative state. This implication appears in writings on price distortions (rent-seeking and directly unproductive activities), state-owned enterprises (patronage and bureaucracy), financial repression (politicized credit allocation and cheap credit to supporters), agricultural markets (pro-urban bias), inflation (populism) and tariffs and quotas (lobbying).

**Predatory (or Leviathan) state**

While the traditional view of the state is that it is a benevolent entity, 'maximising a social welfare function subject to resource and technological constraints', the new political economy views it as 'predatory' (Lal, 1984). Grindle (1991, p. 43) notes, 'recent neo-classical models have helped resolve the clash between theory and empirical observation by replacing the image of the benign state with its mirror opposite, the negative state'. Under the new political economy, regardless of the category the state is assumed to 'prey on its citizens' and promote the interests of the few vested groups at the expense of general public good and social welfare. As North (1979, pp. 250–51) notes, many Social Scientists view the predatory state as:

the agency of a group or class; its function, to extract income from the rest of constituents in the interest of that group or class. The predatory state would specify a set of property rights that maximised the revenue of the group in power, regardless of its impact on the wealth of society as a whole.

A predatory state is not benevolent because it is rent-seeking, it tends to maintain overvalued exchange rates, it taxes trade and promotes a large and inefficient bureaucracy and distributes power and economic gains among a limited number of interest groups. The neoclassicists would like to restrict the activities of the government so that it has fewer resources to squander on these interest groups. The desired outcome of public policy may not occur if rent-seeking is unproductive, if the bureaucrats seek their self-interest and if different interest groups which support public policy exploit the state to their advantage.

**Guardian or platonic state**

In contrast to the predatory state a guardian state is interested in social welfare and the public good. According to Lal and Myint (1996, p. 261), 'instruments of power in the Platonic state have citizen's welfare in their own objective function, whilst in the predatory state the rulers treat their citizens' welfare more as a constraint which restricts their pursuit of other objectives'. This benevolent view of the state is based on a number of premises: first, that governments and civil servants would work for the welfare of the people who themselves might be unaware of their interests; second, that the governments would provide for future

generations better than the poor people who generally have a very high rate of time preference (Krueger, 1993).

The precise outcome of the state or government intervention (the two are used here interchangeably) will depend on a host of factors: relationship between the state and society; convergence or divergence of the interests of the state (and the bureaucrats) and those of the dominant social classes, and the nature of communication between the two groups (Dutt *et al.*, 1994, p. 9). As we discuss in Chapter 2, market failures and inadequacies often justify state intervention which may improve outcomes by promoting competition and by selectively operating through the markets as has been the experience of East Asian economies (Stiglitz, 1994a; Wade, 1990).

Owing to its 'power of compulsion' and 'universal membership', governments may be at a comparative advantage in overcoming market failures (see Stiglitz, 1991b). To quote Stiglitz (1994b, p. 32): 'the government does have powers that the private sector does not have, powers that in certain circumstances... could result in a Pareto improvement' (for example, the case of prohibition of smoking or raising the cost of cigarettes through taxes which no private company could impose).

### **A typology of Third World states**

The above discussion of different types of state shows that different categories overlap. For example, what Myrdal calls the 'hard' state, may not be very different, in its essential features and objectives, from a benevolent state or an autonomous state. Similarly, a factional state may not be very different from a 'soft' state. Essentially, the above categories boil down to (a) dictatorships and (b) democracies with different shades of each depending on the fulfilment of the objective of public good.

In the political literature there does not seem to be a typology of states on a comparative basis. Findlay (1991) presents a rather crude typology of dictatorships and democracy. He notes: 'Democracy versus dictatorship is one axis along which they might be situated, and market orientation and central planning is another, giving us four categories if each of these distinctions is applied dichotomously' (p. 19). Findlay arbitrarily allocates developing countries into 'traditional monarchies', 'traditional dictatorships', 'authoritarian' and 'democratic states'. He links the regime types to public finance strategies but does not present criteria for classifying states into different categories. The Lal-Myint typology discussed above is essentially a grouping of a number of state types into 'autonomous' or 'factional'. Developing countries are classified into

Table 1.2 A typology of Third World states

| <i>Type of state</i>            | <i>Goals</i>   | <i>Legitimacy</i> | <i>Compliance</i> | <i>Participation</i> |
|---------------------------------|----------------|-------------------|-------------------|----------------------|
| <i>Hard or autonomous state</i> | People-centred | High              | High              | High                 |
| – Authoritarian/<br>predatory   | Self-centred   | Low               | Low               | Low                  |
| – Democratic                    | People-centred | High              | High/Low          | High                 |
| <i>Soft or Weak</i>             | ?              | Low/nil           | Low               | Low                  |

either autonomous (further sub-divided into ‘platonic’ or ‘predatory’) or factional (oligarchic and democratic). The authors conclude that in their sample of countries the autonomous states showed superior growth performance to that of factional states.

We present an alternative version of the state typology (based on the above discussion of regime types) in a matrix where columns show state types, and rows, various criteria and goals, namely, legitimacy, compliance and participation discussed in Chapter 2 (see Table 1.2).

Having discussed different types of states, we need to examine in some detail the nature and types of markets in developing countries.

## DIFFERENT TYPES OF MARKETS

There are different ways in which markets have been categorized. First, markets may be defined in terms of the nature of the product or input: thus there are product markets, factor markets or capital and financial markets. The second criterion generally used in economic literature is the degree of price competition: thus markets may be imperfect, oligopolistic or monopolistic. The third interpretation of markets is by non-economists or political scientists who see them as ‘culturally and politically specific’ institutions representing interests of particular social groups. White (1993a, p. 1) notes that the neoclassical economic view of markets deals with an ‘ideal’ type which ignores ‘the social, cultural, political and institutional dimensions of real markets’. Thus, markets represent power relations in the same way as do other pressure groups and governments. Dimensions of market power include the state, association, economic assets and sociocultural status. Sen (1999) discusses the role of markets in terms of freedom to exchange and entry or non-entry into the labour market (for example, non-entry of women and bonded labour as a case of unfree

markets). In discussing markets he suggests that efficiency sought through markets should be accounted in terms of *individual freedoms* instead of *utilities*.

Markets may either function imperfectly or they may function well but in the wrong direction. Basu (1992, p. 341) notes:

The problem with the Indian economy is not that its market is less or more free but that its freedom is in the wrong domains...in some domains the problem is that of *excessive* marketization: there is a price at which everything can be had. In other domains where the market *ought* to be more free, for example, international trade, industry and the entry and exit of firms, our markets are strapped up in bureaucratic red tape.

The above Indian example is mentioned to underline the importance of the right kinds of institutions, social norms and human behaviour for markets to function effectively. Social norms are such that one can buy oneself out of traffic offences and purchase university degrees. When social norms are weak, transaction costs are high, laws may not be obeyed and contract enforcement will be very difficult. Of course, in principle, social norms can be enforced through policing and sanctions, but they may not always explain why an individual does not often default (for example, in making payment to a taxi driver) (Basu, 1986).

In explaining non-market failures, Wolf (1988) cites information acquisition and control becoming an end in itself, leading to influence and power. While he recognizes the role of information in imperfectly competitive markets he concludes that price competition keeps cost inflation in check. However, there are also cases of absence of such competition.

We examine different categories of markets below.

### **Input and product markets**

In economic literature, input and product markets are the most frequently discussed types of markets. The input markets for labour (skilled and unskilled), capital, foreign exchange, land, and so on, and the product markets for consumer goods and intermediate and capital goods are perhaps some of the earliest notions of a market. In conventional neoclassical economic theory, perfect or 'ideal' markets are characterized by perfect competition, complete information freely available to all the agents, and transactions taking place at a price on a self-regulating basis and on the basis of profit motive. Yet in practice,

especially in developing countries, production and dissemination of information is costly and weak because of inefficient institutions. Frequent structural changes make it even more difficult and costlier to collect and disseminate information (Stiglitz, 1997a). Imperfections in the labour, capital and foreign exchange markets (reflected in unemployment, credit rationing, and weak and unstable currencies) are common in most developing countries. As we note in Chapters 3 and 4, financial crises (which are not peculiar to developing countries) are a common form of market failure in open market-oriented economies. The recent liberalization and globalization of financial markets has made it even more common for developing countries with inadequate banking structures, information imperfections and poor institutions and infrastructure, to suffer from vulnerability through external shocks.

### **Competitive or oligopolistic markets**

A competitive market is in equilibrium when supply of and demand for a good or service are equal at a particular price. Thus price mechanism is a self-regulating device. If demand is in excess of supply, price will go up. This will induce producers to raise supply so that a new equilibrium is reached. Milton and Rose Friedman (1980) note three important functions of prices in organizing economic activity and achieving equilibrium: namely, (a) transmitting information, (b) providing incentive to adopt least-cost methods of production, and (c) determining who gets how much of the product. They state: 'One of the beauties of the free price system is that the prices that bring the information also provide both an incentive to react to the information and the means to do so' (p. 33).

The above textbook competitive or 'ideal' market is rarely found in practice. Actual prices do not always reflect scarcities of factors and products, and consumers and producers do not enjoy equal access to information about products and markets. Market failures also occur due in part to lack of informational capacity of economic agents (see Chapter 2). Stiglitz (1994b, p. 105) notes that competitive markets are an exception rather than the rule especially when such non-price factors as contracts and reputation (in allocating capital in capital markets) are important. In such a situation, prices may not be a good indicator of information on supply and demand. Neither are they suitable allocating devices. So prices will not equate marginal costs because rents are bound to persist when reputation mechanisms are at work. Furthermore, competitive markets should not be seen only in price terms; in today's world much of competition is in terms of achieving higher *quality* of products

(product differentiation) or producing better and new products to capture market niches. Barriers to entry and limits to competition may also arise because of the existence of transaction costs (discussed above) including costs of information search and processing, of organization and so on.

The competitive view of markets abstracts from any power relations which determine price at which transactions occur. In contrast to the 'ideal' markets, political scientists have presented the notion of 'real' markets characterized by these power relations (see below).

### **Financial vs. commodity markets<sup>3</sup>**

Financial markets are different from other factor and commodity markets and these markets also differ in different capitalist countries, depending on their historical backgrounds as well as cultural and economic circumstances. To study differences between financial and other markets, it is useful to examine the functions of these markets. In the case of developing countries mobilization of savings for industrialization is considered as one of the main functions of financial markets. But there are other functions besides transferring capital from savers to borrowers, namely, selection of projects, monitoring, sharing and pooling of risks, recording transactions and so on (for a detailed discussion, see Stiglitz, 1994a, 1994b). Unlike commodity markets, financial markets are mainly concerned with information in its various forms: production, processing, dissemination and utilization. The latter markets are more 'imperfectly competitive' (to use Stiglitz's phrase) because they are more information intensive and search: collection and processing of information can be costly.

Two types of information are particularly important in the capital and financial markets: information about the borrower's capacity and promise to pay, and what the borrower is actually likely to pay on some future date (risk of default). Other types of information required relate to (a) *solvency* of financial institutions, which is of interest to investors, and (b) *management* of these institutions, which affects risk and rates of return on investment. The above types of financial information have the character of fixed costs which does not increase with an increase in the volume of lending. In financial markets (unlike the commodity markets), it is not easy to separate (a) exchange transaction, (b) the role of information and (c) risk of default. The price mechanism is unable to provide such information: it is better in matching supply and demand for goods than in matching supply of and demand for loan funds (Stiglitz, 1994a, 1994b). Also as Sengupta (1995, p. 40) states:

of all markets, the market for financial services is most prone to imperfection, and therefore to failure, and that failure occurs because the price of financial services more often than not fails to clear that market.

Although interest rates (prices) do play a role as an allocative mechanism in the sense that they define the opportunity cost of funds, the allocative mechanism is basically a *screening* device in which prices play a secondary role (Greenwald and Stiglitz, 1986). The highest price (interest rate) offered by the borrower does not necessarily mean the highest expected return to the lender because of a possible risk of default which is higher with a greater amount of lending. In financial markets, therefore, *contracts* between borrowers and lenders and *reputations* of the borrowers are far more important for resource allocation than prices. These non-price factors are totally ignored in the neoclassical theory of welfare economics. Yet Stiglitz (1994b, p. 88) notes that contracts are essential in circumstances of incomplete markets. To quote: 'contracts are required because there are simply not "markets" for all the possible commodities . . . and reputations are required simply because we cannot write down all the desired characteristics . . .'. Loan contracts by banks, for example, may include a host of provisions besides the price (interest rate): terms and conditions relating to collateral and risk of default, for example. Thus, unlike the conventional markets where the highest bidder obtains a commodity, in financial market, such an auction system will not work; financial institutions will perform a monitoring and screening function based on knowledge about the potential borrowers and their reputation.

In conventional markets, competition may raise economic efficiency. But in financial markets, this is unlikely to be so; if banks as lenders promote fierce competition they may deprive themselves of repayment of loans from firms that may become bankrupt (Stiglitz, 1994b, p. 222).

### **Free vs. governed markets**

In the context of East Asia, Wade (1990) introduces the concepts of free, simulated and governed markets. Free markets are those in which government intervention is minimal or absent. The role of the government is confined only to the provision of suitable environment for the free functioning of the market. In terms of the trade regimes, Wade (1990, p. 24) notes that the simulated free market theory refers to a situation where 'any incentive for domestic producers to sell on the domestic market rather than export because of protection is offset by export

subsidies'. On the other hand, the free market theory refers to a liberal trade regime with few impediments to imports.

The governed markets refer to markets which are not free but are regulated by the government through a system of controls, incentives and mechanisms. Wade (1990, pp. 26–27) defines the 'governed markets' as follows:

Using incentives, controls and mechanisms – to spread risk, these policies enabled the government to guide or govern market processes of resource allocation so as to produce different production and investment outcomes than would have occurred with either free market or simulated free market policies.

### **Real markets**

A non-economic analysis of markets replaces the price mechanism as an allocational device (used by economists) by power relations between different agents and actors, which may be based on exploitative behaviour or cooperation. As we noted above, real world market functioning is conditioned by social, political and institutional factors. White (1993a) analyzes four major political factors: the politics of (i) state involvement, (ii) market organization, (iii) market structure and (iv) social embeddedness.

The state is involved in markets in different ways: taking over production in the state sector, providing key inputs such as energy to private firms and purchasing agricultural products from the primary producers. These three means of government involvement in the market are common to most developing countries.

Secondly, certain powerful agents, the so-called rent-seekers for example, can exploit the market to their advantage at the expense of other weaker agents. In some cases, cooperation through formal associations and networks may be sought to extract these advantages (see below).

What White (1993a) calls the politics of market structure is indeed within the realm of economic analysis. The monopolistic or oligopolistic market structures discussed above can reflect the economic as well as political muscle of market agents.

Finally, as Polanyi (1957) notes, markets are 'embedded' in wider values and institutions. This may mean that market agents are not necessarily guided by profit maximization or self-interest. Instead, they may be guided by culture, tradition and fairness in regulating market exchange.

It is difficult to develop a neat typology of markets with diverse criteria for classification. What is relevant for our purposes is that markets in actual practice are never perfect since assumptions of perfect competition, zero transaction costs and so on are not valid. As Stiglitz (1994b) notes there is no such thing as 'a complete set of markets'. The imperfections in competition may arise from information costs including fixed costs of obtaining information about how to produce a particular good. Furthermore, 'there are costs associated with establishing a market' (Stiglitz, 1994b, p. 33). Asymmetric information (that is, buyers and sellers have different amounts and types of information) may explain many market imperfections be it in the insurance, equity or labour market. As we note in Chapters 3 and 4, crises in financial markets occur due to information failures and high degree of risk and uncertainty. The well-known problems of adverse selection and moral hazards in the insurance markets (which occur in other markets as well) arise from asymmetric information. Under such situations prices fail to provide complete information, and thus do not clear the market as they should under perfect competition.

## **INTERACTIONS BETWEEN STATE, ORGANIZATIONS AND MARKETS**

The state interacts with markets both directly and indirectly. In a direct manner, the development and control of the public sector – through state corporations, parastatals and nationalized banks, the state participates directly in the market.<sup>4</sup> This is the experience of both China and India which have large state sectors (see Chapter 6). It is also the experience of Africa particularly with the state marketing boards. Bates (1981) shows how government intervention in markets for agricultural commodities, urban goods and factors of production, extracted rural surpluses to finance capital-intensive industrial projects. Indirectly, the state interacts with the market by regulating it. It intervenes mainly to correct market distortions or to strengthen the functioning of the market instead of suppressing it by taking over production.

The development literature on the state briefly reviewed above, takes a very aggregated view of the state. However, in a study of interactions between the state and other non-state institutions, it is more useful to disaggregate the state into its different levels of organization, namely, executive leadership, central agencies, and regional and local bodies (Migdal, 1988, p. 263). Interaction between the state, social organizations and markets is likely to be easier and greater when the state has several levels of organization and when decision-making is decentralized.

Rodrik (1992) argues that an autonomous state leads the private sector and the market whereas the 'subordinate' or 'soft' state (à la Myrdal) would follow it. The latter lacks a 'mechanism that would commit it to reward or punish the private sector according to whether the desired behaviour is carried out or not'. The precise nature of interaction between the two sets of institutions – the state and the market – may depend on the nature of a particular policy action. A policy may be intended to provide an economic incentive (for example, an export subsidy) or to correct a market failure. On the other hand, it may be motivated by a political objective of supporting some powerful groups which may create further market distortions rather than reducing them.

As a free market economy is unlikely to lead to the achievement of social objectives, markets need to be guided to attain these objectives. Datta-Chaudhuri (1990) cites Japan's experience to show that governments can guide the 'perceptions of producers and traders' to exploit their potential which might remain latent under an unguided market economy.

Government also interacts with non-governmental organizations in different ways. Firstly, government may actually create these organizations (as in China) to transfer some of its erstwhile functions. Alternatively, these organizations may provide checks and balances to government interventions. They may also act as lobby or pressure groups to extract gains from the state.

Various associations and organizations also participate in the market as agents representing particular interests. They influence price formation as well as supply of and demand for goods and services. Their role is particularly important in the foodgrains markets in developing countries (Harriss-White, 1993). Institutions such as those of traders and merchants may restrict market entry and control distribution which may not necessarily be socially desirable.

# Author and Name Index

- Agosin, M.R. 49  
Ahluwalia, I.J. 180  
Ahluwalia, M.S. 154  
Ahuja, G. 180  
Akerlof, G.A. 61  
Akyüz, Y. 9  
Amsden, A. 49, 74  
Ardito-Barletta, N. 170, 171, 175  
Arun, T.G. 137, 156, 180  
Auty, R.M. 40
- Bailey, E.E. 34  
Bardhan, P. 6, 12, 156  
Baring, P. 176  
Barlow, C. 11  
Barnes, K. 69  
Basu, K. 7, 17  
Bates, R.H. 22  
Baumol, W.J. 34  
Benston, G. 123  
Berry, A. 48  
Bhaduri, A. 159  
Bhagwati, J. 3, 4, 49, 50  
Bhalla, A.S. vii, viii, 3, 11, 65, 114,  
136, 160, 174, 181  
Bhandari, L. 134  
Bhat, K.S. 180  
Bhole, L. 121  
Bordo, M.D. 51  
Bowers, J. 179  
Boycko, M. 4, 7  
Brass, T. 11  
Breman, J. 73  
Broadman, H.G. 133, 147, 180  
Bruton, H. 167  
Bryant, J. 74  
Buchanan, J.M. 3  
Buitter, W. 158  
Byres, T.J. 11
- Callaghy, T.M. 181  
Calvo, G. 75  
Camdessus, M. 73
- Cao, Y. 136  
Caprio, G. 68  
Chai, J. 103, 178  
Chai, J.C.H. 103  
Chang, H.-J. xiv, 4, 25, 26, 28, 34, 36,  
39, 40, 77, 78, 165, 176  
Chen, K. 142  
Chhibber, P. 155  
Clarke, W.C. 165  
Cline, W.R. 69  
Coase, R.H. 10  
Cohen, I. 174  
Cole, H. 75  
Craig, J. 166, 181
- Datta-Chaudhuri, M. 9, 23  
Demirguc-Kunt, A. 68  
Deppler, M.C. 89  
Desai, A. 178  
Detragiache, E. 68  
Dewatripont, M. 128  
Dholakia, B.H. 156  
Diamond, D.W. 75  
Dollery, B. 25, 28  
Duncan, R. 138, 140, 141  
Dutt, A.K. 10, 15  
Dybvig, P.H. 75
- Edlin, A.S. 5, 7  
Evans, P.B. 1
- Fan, G. 140, 141, 146, 150  
Fei, J.C.H. 130  
Feldstein, M. 81, 82  
Felix, D. 49, 50  
Fernald, J. 93, 110, 117  
Findlay, R. 3, 5, 15  
Fischer, S. 60, 75, 79, 176  
Fisher, I. 74, 75  
Fishlow, A. 9  
Fluitman, A.G. 174, 181  
Friedman, M. 18, 74  
Friedman, R. 18

- Gilley, B. 104  
 Goad, G.P. 85, 86  
 Goldar, B.N. 180  
 Goldsmith, R. 51  
 Goldstein, M. 123, 126  
 Goodhart, C. 56  
 Gore, C. 9, 10, 25, 41  
 Goswami, O. 134  
 Granick, D. 179  
 Greenwald, B. 20  
 Griffith-Jones, S. 50, 52, 59, 61, 176  
 Grindle, M.S. 5, 6, 14, 167, 172, 173  
 Gupta, A.P. 152  
 Gupta, S.P. 159  
  
 Haggard, S. 42  
 Harberger, A.C. 131  
 Harriss, J. 8  
 Harriss-White, B. 23  
 Hay, D. 129, 139, 140, 179  
 Holmes, W.D. 102, 121  
 Howell, J. 10  
 Huang, G. 108  
 Huang, Y. 138, 140, 141, 142, 179  
 Hussain, A. 133, 144, 145, 151  
  
 Jalan, B. 152, 158  
 Jefferson, G.H. 131, 140, 142, 151  
 Jian, T. 180  
 Johnston, B.F. 165  
 Joshi, V. 158, 180  
  
 Kaminsky, G. 52  
 Kaufman, G. 123  
 Kehoe, T. 75  
 Keynes, J.M. 49, 125  
 Khan, M. 79  
 Khan, M.H. 8, 9  
 Killick, T. 79  
 Kindleberger, C. 51, 57, 66  
 Klingebiel, D. 68  
 Knight, J. 131, 147, 148  
 Kornai, J. 127, 128, 129, 130, 161  
 Kregel, J.A. 177  
 Krueger, A.O. 3, 4, 9, 15, 30, 39  
 Krugman, P. 65, 74  
 Kueh, Y.Y. 138  
 Kumari, A. 156  
  
 Lal, D. 2, 13, 14, 15, 39  
 Lapeyre, F. 11  
 Lardy, N. 103, 105, 120, 122, 123, 135, 136, 141, 142, 143, 144, 146  
 Lee, E. 87, 88  
 Lee, P.N. 136  
 Leeson, P. 54, 55, 56  
 Le Grand, J. 29, 31, 32, 33, 43, 175  
 Leibenstein, H. 31  
 Lewis, W.A. 130  
 Li, D.D. 128, 129, 139, 140, 148, 150  
 Liang, M. 128, 129, 139, 140, 148, 150  
 Lim, L. 146, 147, 149, 150  
 Lin, J.Y. 138, 141, 180  
 Lindenberg, M. 181  
 Lipton, M. 163, 175  
 Little, I.M.D. 158, 180  
 Lo, D. 143  
 Loser, C.M. 89  
  
 Majumdar, S.K. 152, 155, 180  
 Makin, J. 93  
 Mao, Zedong 174  
 Maskin, E. 128  
 McMillan, J. 140  
 McNally, C.A. 136  
 Meier, G.M. 2, 3, 13  
 Migdal, J.S. 12, 13, 22  
 Minsky, H. 49, 125  
 Mishkin, F.S. 58  
 Mishra, R.K. 180  
 Mohan, R. 132, 134, 180  
 Morishima, M. 40  
 Motoyama, Y. 178  
 Mundle, S. 157, 181  
 Myint, H. 2, 13, 14, 15  
 Myrdal, G. 12, 15, 23  
  
 Nachane, D.M. vii, viii, xiv, xvii, 65, 92  
 Nagaraj, R. 181  
 Naughton, B. 135, 140  
 Nayyar, D. 159  
 Nelson, R. 170  
 Niskanen, W.A. 29, 37  
 Nixson, F. 73, 137, 156, 180  
 North, D.C. 8, 14, 162  
  
 O'Brien, R. 61  
 Okimoto, D.I. 74  
 Oman, C. 47

- Palma, G. 57  
 Papola, T.S. 159  
 Pareto, V. 15, 26  
 Park, Y.C. 83  
 Patel, U. 158  
 Peacock, A.T. 37  
 Perkins, F.C. 143  
 Polanyi, K. 21  
 Porter, M.E. 36  
 Pratibandla, M. 121, 122  
 Pressman, S. 55  
 Prusty, R. 121  
  
 Qian, Y. 129  
  
 Radelet, S. 49, 71, 73, 76, 100  
 Raiser, M. 128, 140, 143, 149  
 Ranis, G. 88, 130  
 Rao, B.V. 66  
 Rao, M.G. 157, 181  
 Rao, M.J.M. 125  
 Reddy, A.K.N. 3  
 Reinhart, C. 52  
 Rodrik, D. 7, 23, 49, 50, 169, 177  
 Roland, G. 129  
 Rowthorn, R. 28  
 Roy, K.C. 154  
  
 Sachs, J. 49, 71, 73, 76, 100, 143, 144, 150  
 Sankar, T.L. 133, 155  
 Saywell, T. 178  
 Scharfstein, D.S. 50  
 Schwartz, A.J. 74  
 Sen, A.K. 16, 30  
 Sen, T.K. 157, 181  
 Sender, H. 53  
 Sengupta, A. 19  
 Shleifer, A. 128  
 Singh, A. 36, 74, 77, 165  
 Smith, A. 5, 26  
 Smyth, R. 142, 143  
 Song, C-Y. 83  
 Song, L. 131, 147, 148  
 Soros, G. 59  
 Srinivasan, T.N. 3  
 Srivastava, D.K. 157, 181  
 Stern, N. 8, 37, 144, 145  
 Stewart, F. 88  
  
 Stiglitz, J.E. 3, 5, 6, 7, 8, 15, 18, 19, 20, 22, 25, 26, 27, 28, 34, 35, 36, 37, 43, 45, 59, 60, 61, 63, 65, 66, 73, 80, 172, 175, 176  
 Streeten, P.P. 5  
 Sull, D.N. 36  
 Summers, L. 65, 73  
  
 Tam, C.H. 147  
 Thomas, J.W. 6, 167  
 Tisdell, C.A. 154  
 Tiwari, A.C. 157  
 Toye, J. 5  
 Tullock, G. 37  
 Tung, R. 143  
 Turner, P. 123, 126  
 Tussie, D. 49  
  
 Veneroso, F. 59  
 Verma, J.P. 122  
 Vining, A.R. 29, 34, 35, 43  
 Vishny, R.W. 128  
  
 Wade, R. 15, 20, 21, 37, 39, 41, 42, 43, 59, 85, 169  
 Wallis, J. 25, 28  
 Walters, B. 73  
 Wang, Z. 114  
 Weimer, D.L. 29, 34, 35, 43  
 Weiner, M. 166  
 Westphal, L. 41  
 White, G. 16, 21, 181  
 White, L.G. 181  
 Williamson, J. 79  
 Williamson, O.E. xii, 31  
 Wolf, C. Jr. 17, 29, 30, 31, 37, 38, 43, 45, 163, 165, 173, 174, 175  
 Woo, W.T. 140, 141, 142, 144, 150  
 Wu, J. 102  
  
 Xiang, B. 141, 142  
 Xu, X. 146  
  
 Yang, M. 147  
  
 Zhang, W. 136  
 Zhou, X.L. 180  
 Zhu, Rongji 120  
 Zhuang, J. 133, 151

# Subject Index

- accountability
  - criteria of 4, 38
  - definition of 165
  - government 165, 180
  - lack of 45, 152
  - managerial 135
- administrative capacity 169
- adverse selection 22, 26, 58, 62
- Africa 22, 109, 181
- agents 64, 128, 173
- Agricultural Bank of China 102
- Agricultural Development Bank (China) 121
- Alien Business Law (Thailand) 177
- anti-dumping duty 108
- anti-monopoly legislation 5, 10
- arm's-length relationship 74
- Articles of Agreement (IMF) 49
- ASEAN 93, 108
- Asian crisis
  - and capital flows 125
  - and poverty 87–88
  - and the IMF 78–82
  - comparison with the Mexican Crisis 69–73
  - diagnosis 76–78
  - economic & social impact 82–88
  - features 66–69
  - impact on China and India 92–126
  - on rest of Asia 82–88
  - rest of the world 88–90
  - theoretical explanations of 73–76
- asset stripping (China) 136, 142–43
  - and restructuring of SOEs 142, 143
- Association of Science and Technology 10
- Australia 108
- bank
  - bankruptcies 69, 85
  - collapse 25, 37, 62, 63, 162
  - contract 20
  - credit 49, 52, 54, 68, 72, 143, 144, 146, 158
  - domestic 65, 66, 96
  - failures 46, 56, 62, 65, 164
  - foreign 62, 65, 66, 77, 102, 104, 124, 164, 177
  - indiscriminate lending 62, 69, 77, 164
  - liabilities 49, 57, 63, 68, 69, 81, 97, 98
  - loans 47, 98, 101, 102, 139, 143, 144–46, 151–52, 158, 180
  - local 73, 107
  - monitoring and supervision 45, 56, 61
  - offshore borrowing 68, 98
  - portfolio 68, 98
  - private 45, 56, 65, 83, 98, 123, 124
  - recapitalization 81, 120, 123
  - regulation 62, 77, 103
  - runs 46, 52, 60
  - state-owned 98, 99, 102, 104, 120, 123, 128
- Bank for International Settlements (BIS) 52, 53, 54, 58, 63, 64, 68, 71, 97, 100, 101, 102, 123, 126, 177
- Bank of China 102
- Bank of Credit and Commerce International (BCCI) 46
- Bank of England 54, 55, 57
- Bankhaus Herstatt 46
- banking reforms (China) 103
- bankruptcy laws/legislation 78, 103, 105, 160, 164, 173
- Barings Bank 50, 54–56, 57, 58
- Board for Industrial and Financial Reconstruction (BIFR) (India) 137, 159
- Board for Financial Supervision 123
- bonuses 55, 62, 138, 146, 150–51, 160
- bounded rationality 49
- Brazil 51, 59, 90, 117
- Brazilian financial crisis 51, 59, 90

- Bretton Woods 46, 48, 49  
 bubbles and busts 65, 72  
 bureaucrats  
   accountability of 165  
   competent 43, 166  
   maximization of security by 29, 37  
   rent-seeking 29, 37  
   selfish goals of 163  
   technical 43, 66  
 business operations 34
- capital  
   account 47, 49, 118  
   adequacy ratio/target 64, 79, 81, 99, 123  
   controls 40, 47, 48, 49, 50, 60, 96, 125  
   equity 61  
   flight 68, 74  
   foreign 82, 96, 97  
   inflows 46, 48, 50, 65, 66, 67, 69, 72, 77, 79, 82, 85, 91, 93, 96, 97, 100, 101, 110–117, 125, 163  
   market 17, 18, 19, 36, 66, 82, 115, 118, 121, 122, 125, 126, 179  
   mobility 49, 50, 74  
   outflows 40, 46, 66, 77, 80, 85, 90  
   private 59  
   short-term flows 48, 65  
   volatility of 59  
 capital account convertibility 46, 49–50, 58, 66, 91, 124–25  
 capitalism  
   ‘crony’ 77–78, 164  
   Asian model of 77, 78, 82, 164  
   Central Bank (China) 121  
   Central and Eastern Europe 2–3, 85  
   Central Bureau of Statistics (Indonesia) 87  
*chaebols* 79  
 Chile 51, 89, 124  
 China  
   banking reforms 122–23  
   capital account convertibility 124–25  
   commodity composition of trade 106, 109  
   impact of Asian crisis on 100–105, 108–110, 114–117  
   local government in 144  
   privatization in 136  
   soft-budget constraint in SOEs 137–51  
   state-owned enterprises (SOEs) 132–37  
   vulnerability indicators 100–105  
 China Construction Bank 102  
 China International Capital Corporation 115  
 China Venturetech Corporation 119  
 Chinese Academy of Social Sciences (CASS) 114  
 Chrysler Corporation 64  
 Citibank 115, 178  
 Clinton administration 59  
 civil society 10, 11, 165, 175  
 Coca Cola Company 38  
 Colombia 51, 55  
 Commercial Banking Law 102  
 community development movement 166  
 companies  
   finance 98, 102, 177  
   non-bank finance 99, 102, 103, 124, 177  
 Company and Enterprise Laws (China) 136  
 comparative advantage  
   dynamic 39, 41  
   static 39  
 competition  
   absence of 36  
   and economic efficiency 55  
   and profitability 140  
   domestic 152  
   external 104, 107, 152  
   from collective enterprises 32, 152  
   fierce 20  
   global 48, 159  
   imperfect 27, 58  
 competitiveness 18, 41, 83, 100, 109, 158  
   price 18, 109  
   quality 18, 109  
 compliance 12, 16, 81, 171, 181  
 consistency  
   macroeconomic 168  
   microeconomic 168

- of goals 167, 168
- Consortium de Réalisation (CDR)* 56
- consumer
  - behaviour 165
  - choice 165
  - demand 31, 171
  - groups 29
  - preference 2, 3
  - prices 89
  - response 30, 31, 38, 45, 162
- contagion 49, 92, 112, 117
- contestability
  - high 35
  - low 35
  - of government supply 34, 35, 43
  - of government ownership 34, 35
- cooperatives
  - rural 102, 146
  - urban 102, 150
- corporate management 164
- corporation
  - government 35
  - inefficient 77
  - private 35, 36, 74, 77, 171
  - public 173
  - strategy 37
- 'corruption perception index' 176
- cost
  - administrative 172
  - divergence between revenue and 31
  - minimization 31
- credit
  - access to 49, 129
  - allocation 13
  - cooperatives 102, 145
  - excessive domestic 103
  - market 60
  - rating agencies 69
  - rationing 96
  - subsidized 129
  - to the private sector 54, 68, 90, 163
  - unions 104
- Crédit Lyonnais 48, 56–57
- Crédit Suisse 110
- crisis
  - Asian 65–91, 164
  - balance of payments 52, 74
  - banking 46
  - comparison between Asian and Mexican 69–73
  - currency 46, 52, 82
  - debt 46, 48
  - definition of financial 51
  - diagnosis of Asian 76–78
  - features of Asian 66–73
  - financial 45, 46
  - impact of Asian 82–90
  - role of the IMF in Asian 78–82
  - specific examples of financial 54–57
  - unpredictability of 69, 76
- cronyism 77–78, 164
- cross-border flows 47
- currency
  - depreciation 68, 77, 83, 85, 113, 117, 177
  - stabilization 80
- current account 49, 67, 96, 97, 100, 101, 125, 163
- Daiwa Bank 46
- debt
  - crisis 46, 48
  - equity ratio 63, 103
  - external 46, 52, 58, 67, 69, 75, 95, 100, 101
  - internal 72
  - long-term 57, 58, 69
  - management of 58
  - rescheduling of 72, 76, 102
  - restructuring of 76
  - self-fulfilling crises 75
  - servicing 46, 57, 100
  - short-term 57, 58, 72, 75, 101, 102, 105
  - 'triangular' (China) 102
- decentralization
  - administrative 171
  - by multinational corporations 171
  - of decision-making 103, 171
  - regional 129, 144
- deficit
  - budget 41, 74, 101, 103, 143, 151
  - current account 67, 72, 94, 96, 101, 163
  - fiscal 79, 94, 96, 97, 137

- delegation of power 166
- democracies 15
- Department of Company Affairs (India) 121
- deregulation 6, 47, 48, 60, 118, 158
- derivatives 55, 59, 61, 63, 176
- devaluation 46, 73, 80, 83, 85, 93, 100, 107, 109–110, 113, 178
- Development Research Centre of the State Council (China) 102
- dictatorship 15
- Disinvestment Commission (India) 137
- Dissemination Standard Bulletin Board (DSBB) 60
- East Asia
  - economies 20, 43, 58, 89, 164, 168, 169
  - experience with government implementation 39–42
  - policy 42
  - positive role of government 39–42
- East Asian miracle 39
- economic agents
  - information capacity of 18
- Economic and Political Weekly* (EPW) Research Foundation (India) 122, 134, 177
- Economic Planning Agency (Japan) 40
- economic reforms
  - banking sector 93
  - financial 93
  - future of 117–21
- equity
  - allocative 25, 27, 32, 33, 136, 175
  - and equity 163
  - dynamic 25, 27, 41, 175
  - economic 20, 127, 131, 134, 141, 148
  - index 141, 155
  - productive 27, 32
  - X-efficiency 27, 32, 175
- embedded autonomy 43
- employment elasticity of output 159
- enforcement
  - administrative cost of 4
  - contracts 17, 162, 163
  - mecahnisms 162
  - of property rights 42
  - of rules 12–13
  - public 161
  - regulations 165
  - strategy 24
- Enron Corporation (USA) 86, 113, 178
- enterprises
  - collective (China) (COEs) 32, 133, 136, 139, 140, 142, 148, 149, 152, 180
  - departmental (India) 132, 157
  - foreign 114
  - level of control and supervision (China) 132, 133, 151
  - local 179
  - non-departmental 132, 157
  - ownership of 134, 135
  - private 64, 130, 132, 149, 154, 155, 158
  - profitability 148
  - public sector (India) 132–37, 151–60, 180
  - rural 32
  - ‘sick’ (India) 137, 154, 156, 157, 158, 159, 160
  - state-owned 103, 104, 132–37, 138–51, 152, 156, 180
  - surveys 140, 146, 150
  - town and village (TVEs) (China) 133, 140, 142, 148, 150, 180
- Environmental Protection Agency (EPA) (USA) 38
- equity
  - and efficiency 25
  - blindness 11
  - criteria 32
  - distributional 25, 29, 36, 38, 41
  - to-asset ratio 102, 105
- Euromoney Country Risk Assessment 69
- Europe 86
- European Monetary System (EMS) 46
- European Union (EU)
  - and anti-dumping duties 108
  - and the Asian crisis 89, 109
  - rules 54
  - trade with China 109

- trade with Southeast Asia 109
- excess labour 28, 90, 127, 130–32, 146–49, 158–60
- exit policy (India) 158, 160, 161
- expectations
  - change in 51
  - investor 76
  - overshooting of 76, 77
- export
  - cheap 93, 100
  - Chinese 106, 108–110
  - commodity composition of 109
  - competitive 83, 93
  - decline in 84
  - earnings 81
  - extra-regional 82
  - growth 83, 95, 101, 105, 108, 109
  - import-intensive 83, 107
  - income elasticity of 107
  - Indian 105–108
  - intraregional 82, 84
  - Japanese 84
  - Latin American 89
  - licences 109
  - market 42, 93, 119
  - promotion 40
  - recovery 73
  - revenue 89
  - share 93
  - stagnation 73
  - subsidy 20–21, 23
  - targets 168
  - tax refund system 109
  - value 83
  - volume 84, 110
- Exports and Imports Bank (China) 121
- externalities
  - cause of market failure 7, 25, 60
  - 'derived' 37, 38
  - environmental 11
  - in financial markets 60–61
  - negative 26, 60
  - positive 26
  - problems of 27
- failures
  - fiduciary theory of government 34–36
  - in financial markets 90
  - in implementation 162–74
  - Le Grand's theory of
    - government 31–34
    - market xiii, 25–28, 64,
    - non-market xiii, 28–36
    - parallels between market and government 37–38
    - private corporate sector xiii, 1, 36, 64
    - sources of 30–31
    - systemic 64, 77
    - Wolf's theory of government 29–31
- Farmers' Movements (India) 11, 175
- feasibility
  - and political expediency 168
  - of implementation 168–69
- FDI Confidence Index Survey 117
- financial crises
  - cases of market failure 45–64
  - industrial and developing countries 50–57
  - lessons from 63–64
- Firestone Company 36
- firms' entry and exit 154
- fiscal prudence 44, 100
- flexibility
  - built-in 168
  - labour market 149
  - long-term 41, 168
  - of government policy 168
  - short-term 41
- forecasts
  - economic 69
  - export 107
  - IMF 86, 105
  - of GDP growth 86
- foreign exchange
  - controls 47
  - crises 90
  - transactions 47
- Foreign Institutional Investors (FIIs) 122, 179
- Foreign Investment Promotion Board (India) 178
- France 38, 48
- freedom
  - individual 17
  - political 171

- freedom – *continued*  
 to exchange 16  
 free-rider problems 10
- gainers and losers 173
- globalization  
 economic 7, 11  
 financial 18, 46, 47–48, 61, 88
- Goldman Sachs 53, 69, 95, 97, 177
- governance  
 global 1, 9  
 national 1, 9
- government  
 checks and balances on 10, 23, 30, 38, 165, 170  
 –corporation axis 77  
 democratic 37  
 expenditure policy 36  
 informational capacity of 26, 27  
 intervention 1, 4, 7, 9, 15, 22, 23, 31, 38, 39, 41, 43, 44, 57, 74, 126, 163  
 local 103, 128, 129, 133, 144, 146, 149, 179, 180  
 market interactions 42–43  
 monopoly 32  
 ownership 32  
 positive role of 39–42  
 powers of compulsion 15, 35, 43  
 production 34  
 quality 10  
 regulation 33, 34, 43  
 subsidies 27, 31–32, 33, 35, 36, 43, 77, 143–44, 151, 152, 156–57  
 supply 34, 35, 43  
 tax revenue 139  
 universality 15, 35, 43
- government failures  
 fiduciary theory of 34–36  
 parallels with market 37–38  
 relevance of theories to East Asia 38–43  
 theories of 28–36
- Green Revolution 11, 36
- Group of Ten countries 64, 177
- growth  
 and equity 1  
 Chinese 101  
 Indian 94  
 of GDP 66, 95, 101, 105
- Guangdong International Trust and Investment Corporation (China) 119
- Hainan Development Bank (China) 102, 104, 119
- hard-budget constraint 130, 131, 133, 138, 148, 149, 150, 161, 164, 179
- Hong Kong 59, 66, 78, 88, 89, 105, 106, 107, 108, 114, 115, 177, 178
- hot money flows 49
- Imperial Chemical Industries (ICI) (UK) 178
- implementation  
 complexity of 163, 170  
 design 166–69  
 factors affecting 169–74  
 failures 24, 28, 41, 127, 162–74  
 feasibility of 168–69  
 interactive model of 167  
 linear model of 167  
 of private corporate strategy 24, 25, 162, 167  
 organizational/administrative capacity for 169  
 policy 24, 162, 163, 167, 169, 174  
 quality 170  
 reforms 118, 166, 172, 173  
 strategy 162, 166, 167
- import-substitution 40, 47, 119
- incentives 8, 33, 35, 36, 43, 62–63, 123, 126, 144, 149
- independent accounting units (China) 141, 180
- India  
 banking reforms 123–24  
 capital account convertibility 124–25  
 impact of Asian crisis on capital inflows 110–114  
 privatization in 137, 155–56, 158, 180  
 public-sector enterprises (PSEs) 132–37, 151–61  
 soft-budget constraint in PSEs 151–61

- trade impact of Asian crisis
  - 105–108
- trade composition 106
- indicators
  - financial 70–71
  - human development 87
  - macroeconomic 57, 95
  - vulnerability 94–105
- Indonesia 51, 52, 53, 54, 58, 66, 68, 69, 70, 72, 79, 80, 81, 82, 83, 84, 85, 86, 87, 88, 105, 106, 107, 176, 177
- Industrial and Commercial Bank (China) 102, 104
- Industrial Disputes Act (India) 160
- inefficiency
  - allocative 27, 32, 33, 35
  - corporate 36
  - dynamic 26, 27, 32, 33
  - exchange 26
  - product-mix 26
  - production 26
  - productive 26, 27, 32
  - static 32
  - X- 27, 31, 32, 33, 35, 130, 175
- infant industries 41
- inflation 13, 48, 67, 87, 88, 95
- information
  - acquisition 19, 43
  - asymmetric 22, 38, 49, 58, 127, 128, 138
  - capacity 58
  - collection 19, 172
  - complete 22
  - constraints 22, 172
  - cost 19, 22, 27, 36
  - disclosure 58, 59, 62
  - dissemination 18, 27, 43, 172
  - failures 26–27
  - imperfections in monitoring 57–60
  - intensive 19, 58
  - perfect 22
  - processing 19, 172
  - production 18, 19, 27
  - types of 22
  - utilization 19
- infrastructure
  - expenditure 93, 94, 101
  - institutional 28
  - intellectual (human) 28, 42
  - physical 28, 42
- institutional factors 8, 162, 170, 173
- institutions
  - and organizations 8–11
  - banking 129
  - cooperation between government and market 42
  - financial 20, 48, 51, 52, 57, 61, 103, 104, 118, 119, 123, 162
  - global 64
  - management of 57, 58
  - market 9, 162, 167
  - new 8
  - non-bank financial 99, 103, 124
  - non-market 9, 167
  - non-viable 80
  - private 8
  - public 8
- interactions
  - government–market 42–43
  - between government and social organizations 22–23
- interest groups 4, 5, 6, 169, 173
- Interim Committee (IMF) 49, 60
- International Chamber of Commerce (ICC) 113
- International Finance Corporation (IFC) 116
- International Institute of Finance (Washington DC) 85
- International Labour Office (ILO) 87, 147, 149, 158, 159
- International Monetary Fund (IMF) 47, 50, 51, 52, 59, 60, 66, 71, 72, 73, 75, 76, 77, 78, 79, 80, 81, 82, 83, 86, 87, 88, 89, 90, 95, 97, 101, 105, 106, 111, 125, 176
- and capital account
  - convertibility 125
  - and the Asian crisis 78–82
  - as lender of last resort 59, 75
  - bailouts 75, 77
  - disclosure of information by 60
  - firefighting strategy 79
  - forecasts 86, 105
  - policies/ programmes 79, 80, 81, 179
  - restructuring of operations 59
  - standby agreements 78, 173

- investment
  - cartels 40
  - domestic 68
  - foreign direct 47, 72, 85, 92, 96, 97, 100, 110, 111, 113, 114, 117, 176, 177
  - foreign portfolio 47, 72, 78, 92, 97, 110, 111, 112, 118
  - indivisibility of 36
  - volatile 47
- Japan 25, 38, 39, 40, 41, 42, 51, 53, 54, 67, 73, 78, 82, 84, 86, 105, 106, 107, 108, 114, 124, 169
  - exports to affected Asian economies 84
  - recession in 73
- job security 74
- joint-stock companies 135, 136, 147
- joint ventures 133, 137, 149, 176, 178
- Kodak 115
- Korea, Republic of 38, 39, 40, 41, 42, 49, 53, 54, 58, 66, 67, 68, 69, 70, 72, 74, 78, 79, 80, 81, 83, 84, 85, 86, 87, 88, 93, 106, 107, 108, 168, 169, 176
- labour
  - bonded 16
  - entry into market 16
  - (market) flexibility 149
  - hoarding 131, 132
  - laws/legislation 40, 132, 160, 164, 173
  - local bureaus (China) 148
  - management relations 156
  - market 22, 27, 40, 147, 149
  - mobility 149
  - opportunity cost of 35, 131
  - productivity 130, 131, 150, 151
  - quality 150
  - redeployment 130
  - service companies (China) 146
  - surplus 130–32, 146–50
  - zero marginal product of 131
- laissez-faire* 6, 9, 10, 39, 48, 50, 65, 118
- Latin America 46, 59, 85, 89, 90, 109
- Laura Ashley 36
- legitimacy
  - political 16, 169
- legitimation 12
- liberalization
  - FDI 118, 176–77
  - financial 46, 48–49, 60, 63, 78, 92, 103, 104, 120
  - market 2
  - policies 5, 48–49
  - price 141
  - trade 118, 119, 120
- loan
  - bad 52, 103, 105, 120, 122, 123
  - default on payment 19, 20, 62, 174
  - non-performing 51, 52, 53, 102, 103, 105, 120, 144, 158
  - ‘non-Plan’ (India) 152
  - policy 144, 146, 161
  - private 47
  - ‘soft’ 145, 161
- lobby 23, 173
- losses (enterprise)
  - operational 138
  - policy-induced 138
- macroeconomic (mis)management 65, 67, 68, 74, 76, 90, 163
- macroeconomic (in)stability 41, 44, 48, 50, 62, 143
- Malaysia 41, 51, 52, 53, 54, 58, 66, 68, 69, 71, 72, 78, 81, 83, 84, 85, 86, 98, 99, 106, 107, 114, 177
- managerial stubbornness 36
- ‘mania, panic and crash’ 57
- market
  - absence of 6, 25
  - and power relations 21
  - as cultural and political institutions 21
  - capital 17, 18, 19, 36, 66, 82, 115, 118, 121, 122, 125, 126, 179
  - commodity 19–20, 45, 58, 64
  - competitive 18–19
  - deregulation of 62

- dichotomy between state and 11, 163, 166
- different types of 16–17
- disequilibrium 27
- distortions 22, 25, 27–28, 44, 47
- equilibrium 18
- exchange 21
- factor 9
- financial 19–20, 45, 60, 61, 64, 163
- foodgrains 23
- foreign exchange 18
- free 20–21
- futures 55
- global capital 82
- governed 20–21
- guided 23
- ideal 17
- imperfections 6, 16, 25, 27, 44, 61–62, 142
- incomplete 20, 25
- inefficiency 27, 35
- input 16, 17–18
- interaction with state and organizations 22–23
- labour 17, 18, 27, 60, 88
- monopolistic 16, 21, 142
- oligopolistic 16, 18–19, 21
- organization 21
- power 16, 21
- product 9, 16, 17–18, 150
- protagonists 35
- real 19, 21–22
- structures 21
- typology of 22
- unfree 16–17
- market failures
  - and government intervention 1
  - conventional 25–26
  - in financial markets 57–63
  - non-conventional 26–28
  - theories of 25–28
- maximization
  - income and employment 37
  - of labour productivity 131
  - output 131
  - profit 29, 131, 132
  - rent 37
  - utility 29, 37
  - vote 29
- Memorandum of Understanding (India) 180
- mergers and acquisitions (M&As) 113, 115, 179
- Mexico 48, 51, 53, 54, 72, 73, 124
- Mexican crisis 46, 48, 50, 51, 60, 76
- Ministry of International Trade and Industry (MITI) (Japan) 40
- monetary policy 60, 67, 74, 79, 103, 107, 171
- monitoring 19, 20, 36, 48, 56, 57, 58, 60, 61, 63, 83, 128
- Moody's Investors Service 69, 82, 97, 103
- moral hazards 22, 26, 58, 61, 77, 96, 104, 122, 124, 138
- multinational corporations 5, 37, 47, 85, 89, 100, 112, 113, 162, 171
- NAFTA 73
- National Renewal Fund (India) 159
- Nikkei futures market 55
- non-bank finance companies (NBFCs) 99, 124
- non-market failures (*see also* government failures) 17, 29–31, 45, 163, 175
- non-price factors in financial markets 18, 20, 61
- non-production workers 140, 147
- non-tradeables 53, 96
- norms
  - legal 7
  - social 7, 8, 17, 166
- objectives
  - conflicting 168
  - economic 128, 160
  - equity 163
  - feasibility of 167
  - formulation of 37
  - multiple 36, 131, 168
  - non-economic 127, 128
  - political 23
  - social 41
- opposition groups 172–73
- organization
  - administrative 171–72
  - local 165, 166

- organization – *continued*
  - non-governmental 23
  - private 37, 163
  - profit-maximizing 32
  - public 37
  - social 10–11, 38
- Organization for Economic Cooperation and Development (OECD) 86
- Osaka Stock/Securities Exchange 55, 176
- overborrowing 57, 66, 101
  - by domestic banks 66
  - by foreign banks 66, 101
- overlending 57, 66
- overstaffing 24, 30, 44, 127, 130–32, 146–50, 151, 154, 158–60
- panic
  - bank 49, 74
  - financial 49, 57, 60, 74–75, 76, 78, 90, 164
  - theories of bank 74–75
- Pareto optimality 15, 26
- participation 16
  - in negotiations 170
  - in policy formulation 165, 170
  - local 165
  - popular 10, 16, 38, 170
  - political 170
- People's Bank of China 103, 119
- Peru 89
- Philippines 51, 53, 54, 58, 66, 68, 69, 71, 72, 73, 83, 84, 86, 87, 106, 107, 177, 178
- picking winners 37, 42, 178
- policy
  - administration-intensive 173
  - checks and balances on public 38
  - content of 168
  - domestic 92–93
  - feasibility of implementation 168–69
  - financial liberalization 48–50
  - formulation of 164, 169
  - impact of domestic 117
  - implementation of 163, 164, 169
  - incomes and wages 40
  - industrial 40, 44, 77, 78
  - macroeconomic 171
  - optimal 168
- political economy
  - a critique of new and old 6–8
  - comparison with new 2–6
  - features of 1–8
  - new 1, 2, 3–6
  - old 1, 2
- political pressures 42, 144, 181
- political systems/regimes
  - autocratic 171
  - democratic 12, 15, 16, 30
  - dictatorial 12, 15
  - nature of 170–71
  - one-party 170
- politicians
  - rent-seeking 29
  - vote-seeking 29, 42
- poverty
  - alleviation 7
  - decline in 87
  - increase in 87, 88
  - new 11
- precautionary loan package (IMF) 59
- pressure groups 23, 30, 38, 165, 173
- price
  - as allocative device 18, 20, 21
  - asset 51, 53, 72
  - below-market 141, 143
  - commodity 67, 89, 90
  - controls 129, 141
  - dispersion 27
  - distortions 4, 9, 27
  - formation 23
  - semi-conductor 67
  - wars 40
- principal–agent problem 58, 64, 127, 128, 138, 142, 143, 164, 165
- Private Entrepreneurs' Association (China) 10
- privatization 7, 34, 118, 119, 120, 135, 136, 137, 155, 156, 158, 159, 161, 164, 180
- private sector 4, 6, 9, 23, 25, 37, 45–46, 54, 62, 65, 68, 96, 98, 129, 136, 137, 155, 156, 158, 159, 162, 164, 169, 172, 175
- privilege 38

- production
  - cost 152
  - non-market 7
  - public 41
  - state control of 3
  - subsistence 3, 7
- productivity
  - capital 156
  - labour 130, 131, 149, 150, 155, 160
  - maximization of 131
  - partial 142, 156
  - total factor 142, 156
- profitability
  - as index of efficiency 155
  - of state enterprises 138–42, 148, 153–56
  - of collective enterprises 140, 148
  - of town and village enterprises 140, 148
- profit retention scheme 134, 135, 136
- property rights 7, 14, 28, 34, 42, 142
- public choice theory 28
- public goods 7, 25–26, 34, 131
- public policy
  - society-centred 5, 172
  - state-centred 5, 172
- public provision 41
- public-sector enterprises (India) 119, 151–60
  - and soft-budget constraint 151–54
  - bank loans to 151, 157, 158
  - economic performance of 152, 155
  - in developing countries 36
  - loss-making 155
  - pricing policy of 36
  - privatization of 155
  - profitability of 154–56
  - restructuring of 137
  - subsidies to 156–58
- purchasing power parity 74
- real effective exchange rate 67, 96, 97, 163
- reforms
  - banking sector 122–24, 126
  - capital market 121–22, 126
  - financial 121–25
  - future of 117–21
  - sequencing of 118
- regulation
  - bank 62
  - economics and politics of 31–33
  - enforcement of 63
  - external 56
  - internal 56
- regulators
  - cooperation between 63
  - external 63
  - futures 61
  - internal 63
  - stock market 61
- regulatory mechanism/device 48, 50, 60, 62
- rent-seeking
  - and administrative cost of policy implementation 172
  - government/ bureaucrats 2, 4, 9, 13, 14, 35, 37, 39, 172
  - in the private sector 4, 21, 172
  - positive aspects of 4
  - through trade restrictions 4
- reputation mechanisms 18, 20
- Reserve Bank of India 95, 97, 99, 100, 107, 111, 117, 123, 124, 179
- resource
  - allocation 1, 20, 21, 24, 27
  - constraints 173–74, 181
  - creation 4
  - efficiency 25
  - organizational/managerial 173
  - utilization 173
- restructuring 52, 120
- retrenchments 87, 120, 146–47, 159
- risk
  - control management 56
  - diversification 172
  - financial 46
  - management procedures 54
  - of loan default 19, 20, 60, 62
  - premium 98, 104
  - sharing 75
  - taking 57, 61, 62–63, 64
- rules and regulations 162, 165, 166
- Russian crises 59
- sanctions
  - economic 93
  - social 8, 17

- Scandinavia 52
- Self-Employed Workers' Associations  
(China) 10
- shareholders 36, 58, 104, 113, 118,  
121, 136, 163–65
- Sick Industrial Companies Act  
(India) 137, 158
- SIMEX (Singapore) 54, 55, 176
- Singapore 56, 85, 88, 93, 107, 114,  
177
- social embeddedness 21
- social safety net 87, 159
- social welfare 2, 3, 10, 14, 37, 39, 103,  
130, 137, 138, 149, 152
- soft-budget constraint 33, 44, 61,  
103, 127–30, 133, 137, 138, 139,  
140, 142, 145, 150, 151–52, 158,  
161, 163, 179
- concept 127–30
- indicators of 130
- measurement the extent of 130
- solvency of financial institutions 19
- South Centre 47
- Southeast Asia 44, 45, 52, 57, 58, 65,  
66
- Spain 51, 52
- Special Data Dissemination Standard  
(SDDS) 60
- stabilization policies/programmes 2,  
88
- Standard & Poor 69, 82, 97
- state
- absolutist 13
  - access to the 5
  - agents of the 2
  - as rational entity 2
  - authoritarian /bureaucratic 13,  
15
  - autonomous 13, 15, 16, 23
  - capability 12
  - checks and balances on 10, 23
  - 'civil association' view of the 2
  - democratic 12, 15, 16
  - dictatorial 12, 15
  - different types of 7, 12
  - 'enterprise' view of the 2
  - extent 10, 12
  - factional 13, 15
  - fiduciary responsibility of 35
  - guardian 13, 14
  - hard 12, 15, 16
  - interaction with markets and  
organizations 22–23
  - intervention 12, 15
  - Leviathan 14
  - minimalist 3
  - overextended 2, 13
  - Platonic 14, 16
  - predatory 13, 14, 16
  - redefining the role of 2
  - relationship with society 15
  - soft 12, 15, 16, 23
  - subordinate 23
  - typology of Third World 15–16
- State Development Bank (China) 121
- State Economic and Trade Commission  
(China) 121, 139
- State Electricity Boards (India) 154,  
155
- state-owned enterprises (China)
- and profitability 138–42
  - and overstaffing 146–50
  - and soft-budget constraint 137–38
  - autonomy of 136
  - bankruptcies 143, 146, 150
  - debt–asset ratio of 136, 139
  - economic performance of 142, 164
  - leasing of 136
  - losses of 138, 139, 140, 141, 143,  
145, 147, 152
  - policy burdens of 138, 140
  - sale of 136
  - state bank loans to 144–46
  - state subsidies to 139, 143–44, 145
  - wages and bonuses of 150–51
- State marketing boards 22
- State Science and Technology  
Commission (China) 101
- Statutory Liquidity Ratio (SLR) 95
- stock market
- booms 112
  - busts 65
  - Chinese 115, 116
  - Hong Kong 115
  - Indian 110, 116, 121, 179
  - speculation in 117
- strategy
- corporate 167

- design 166–69
  - private 167
  - public 167
- structural adjustment policies/
  - programmes 2, 48, 73, 78, 90
- structural changes 18, 27, 79, 173
- Structured Early Intervention and Resolution (India) 123
- subsidies
  - direct 143, 144, 152, 157
  - indirect 143, 144, 145, 152, 157, 158
  - price 144
    - state 143, 144, 154, 156, 157
- swadeshi* philosophy (India) 119
- Taiwan 38, 39, 40, 41, 42, 49, 53, 88, 93, 108, 114, 124, 169
- Tarapore Committee (India) 125
- target
  - groups 168
  - implementation 174
  - monitoring of 174
  - plan 135
  - qualitative 174
  - quantitative 174
- Thailand 51, 52, 53, 54, 58, 66, 68, 69, 70, 72, 78, 79, 80, 82, 83, 84, 85, 86, 87, 88, 107, 177
- theories
  - of government failure 28–29
  - market 25–28
  - non-market failures 29–31
  - relevance to East Asia 38–43
- Third World 15–16
- Tokyo Stock Exchange 176
- tradeables 47, 96
- trade unions
  - opposition from 159
  - power of 42, 132, 181
  - pressures 161
- transaction costs 8–9, 10, 17, 19, 22, 61, 162
- Transparency International 176
- Trust and Investment Companies (China) 102
- UNCTAD 47, 52, 58, 84, 85, 86, 90, 111, 113
- UNDP 170
- UNECLAC 89
- unemployment 25, 27–28, 86, 87, 88, 89, 137, 161
  - benefits 87, 148
  - disguised 137, 149
  - insurance 149
- United Kingdom 38, 50, 55, 57, 58, 74, 105, 107
- United States 38, 46, 50, 51, 53, 54, 59, 67, 74, 81, 82, 86, 89, 93, 106, 107, 108, 109, 117, 124
- unproductive activities 3, 5, 13
- urban collectives (China) 146
- Urban Land Ceiling Act (India) 160
- vested interests/groups 6, 14, 29, 30, 169, 173, 175
- volatility
  - and macroeconomic instability 48, 59
  - and market trading 112
  - causes of 46
  - dangers of 48
  - exposure of national policies to 48
  - index 47
    - of asset prices 48
    - of capital inflows 59, 78, 92
    - stock market 112
- Voluntary Retirement Scheme (India) 159
- vulnerability
  - country's 92
  - financial (sector) 60
  - indicators/index 94–105
  - of China/India to the Asian crisis 92
  - of the banking sector 49, 52
  - of women 88
  - through external shocks 18
  - to panics 49
- wage
  - and bonus payments 158–61
  - and incomes policy 40
  - bargaining 151
  - bill 150, 180

wage – *continued*

by level of administrative  
control 151  
determination 35, 151  
falling real 86, 87  
increase 150  
legislation 33  
of state-enterprise workers 150,  
151, 160  
policy 40, 160  
share 151

Wall Street 50

World Bank xii, 2, 9, 39, 41, 59, 85,  
86, 87, 88, 95, 111, 114, 117, 122,  
136, 139, 140, 144, 147, 150, 177,  
180

WTO 99, 125

X-inefficiency (*see also* productive  
inefficiency) 33, 130

*xiagang* (lay-offs) 147–48